STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 98-781

October 14, 1998

PUBLIC UTILITIES COMMISSION
Investigation of Standard Offer
Rate Design

NOTICE OF INVESTIGATION

WELCH, Chairman; NUGENT and DIAMOND, Commissioners

I. SUMMARY

Through this Notice, we initiate an investigation to establish standard offer rate design for each transmission and distribution (T&D) utility service area.

II. BACKGROUND

Maine's electricity restructuring law (the Act) requires that standard offer service be available to all Maine consumers when retail access begins. 35-A M.R.S.A. § 3212. The Act directs the Commission to establish terms and conditions for standard offer service, and further directs that the service be acquired for Maine consumers through a Commission-administered competitive bid process.[1] On February 11, 1998, the Commission provisionally adopted rules establishing the terms and conditions for standard offer service and the provisions governing the competitive bidding and selection process. *Order Provisionally Adopting Rule and Statement of Policy Basis*, Docket No. 97-739 (Feb. 11, 1998). Pursuant to the requirements for major substantive rules, the Commission submitted the provisionally adopted rules to the Legislature. The Legislature enacted a resolve modifying several provisions of the rules. On April 22, 1998, the Commission finally adopted Chapter 301.

Among the issues addressed by Chapter 301 is standard offer rate design. Specifically, Chapter 301 provides that:

> Rates for standard offer service shall be a uniform percentage, across and within classes, of each unbundled generation rate element of the core customer classes of the transmission and distribution utilities, as established by the Commission . . .

Ch. 301, § 2(A)(3).

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[1]The Act was later amended to allow consumer-owned utilities to conduct the standard offer bid process for their service territories. 35-A M.R.S.A. § 3212(6).

Chapter 301 anticipates that these unbundled generation rate elements will be established pursuant to processes and timing set forth in a separate rule, Chapter 309, which governs the unbundling of generation for the purpose of illustrative unbundled bills. Chapter 309 requires the Commission to establish generation rate elements for standard offer rate design prior to August 1, 1999, and allows the Commission to draw from findings made or information provided in other proceedings, or to conduct a separate proceeding. This investigation will serve as the procedural vehicle for setting generation rate elements for purposes of standard offer rate design.

The proceedings for the aforementioned rules elicited substantial and constructive input on a variety of policy and technical issues; however, we received little substantive comment on standard offer rate design. We consider the issue of standard offer rate design to be significant. It has consequences for electric rate stability and, possibly, the design of T&D rates, as well as for the effective operation of the market. We also expect it to be important to potential standard offer providers in their efforts to match standard offer revenues to underlying costs. Accordingly, we initiate this proceeding for three purposes: (1) to provide an additional opportunity for comment on the approach to standard offer rate design; (2) to resolve implementation issues; and (3) to establish unbundled generation rate elements. In addition to the approach set forth in Chapter 301, we note and seek comment on an alternative approach recently proposed by Central Maine Power Company (CMP) in its ongoing rate proceeding, *Investigation of Central Maine Power Company's Stranded Costs, Transmission and Distribution Utility Revenue Requirements and Rate Design*, Docket No. 97-580, whereby providers, through the bid process, would determine standard offer rate design. We seek comment on the merits of provider-determined standard offer rate design vis-a-vis the administrative approach contained in Chapter 301.

III. DISCUSSION

As noted above, the Act requires a competitive bid process to select providers for standard offer service in Maine. We believe this embodies the Legislature's desire that standard offer rates be as low as possible, but not artificially low so as to foreclose entry into Maine's electricity markets by non-standard offer competitive providers. In developing Chapter 301, the Commission reflected two additional objectives. First, from a customer's perspective, standard offer should resemble traditional electric service. That is, when T&D and standard offer service and rates are combined, a customer should receive electric service that appears similar in many respects to

current, bundled service. Second, the procurement process for standard offer supply should be simple and allow bids to be compared easily and objectively. The extent to which we achieve these objectives depends to a large degree on our decisions regarding standard offer rate design.

There are other considerations that may also be relevant to standard offer rate design. These include the cost structures of potential suppliers, how closely rates should track these cost structures, and the relationship between standard offer and T&D rate design. We discuss these within.

IV. DESCRIPTION OF APPROACHES; REQUEST FOR COMMENT

Chapter 301 provides that standard offer usage components, and the variance among components and customer classes, be determined by the Commission. The Commission would establish, for instance, whether standard offer customers would pay demand charges, or whether they would pay kWh charges only. The Commission would also establish the variance, if any, of standard offer rates from one class to another. The rationale for this is twofold: first, it allows the Commission to manage rate stability; second, it allows the Commission to evaluate competing standard offer bids objectively. An alternative approach recently put forward by CMP in its ongoing rate proceeding would leave this discretion with standard offer providers; potential providers would propose rate designs, as well as rate levels, as part of the competitive bid process. We describe each approach in more detail below and ask for comment on how well each approach complies with the objectives set forth above, and on whether the approach is reasonably practical to administer.

A. Chapter 301 Approach

1. Description

The Chapter 301 approach requires the Commission to set generation rate elements for the core customer classes of each T&D utility. In effect, these rates are a template for standard offer rate design. Each standard offer bidder would propose a single percentage (e.g., 90%, or 105%) that, when applied to the template rates, would be its proposed prices for standard offer service. For example, for a T&D utility with the following template:

For Class A: $.0400 per kWh

For Class B: $4.00 per kW
$0.0250 per kWh

and standard offer bid of 90%, standard offer prices would be:

For Class A: $.036 per kWh

For Class B: $3.60 per kW
$0.0225 per kWh

The winning bid(s) would be determined by simple comparison of the percentage amount each bidder proposed. If more than one supplier was chosen to provide service, standard offer rates would be a weighted average of the suppliers' bids. We describe below an administrative approach to establishing standard offer rate design consistent with the terms of Chapter 301 and seek comment on the approach.

To establish the generation rate elements, the Commission would estimate market-based generation costs corresponding to applicable usage components in each core customer class of each utility. This is so the structure of standard offer rates will reflect market generation costs as closely as practicable thereby minimizing mismatches between supplier revenues and costs.[2] This is particularly important given the uncertainty regarding customer composition and sales levels under standard offer. For classes that currently pay only kWh charges (no demand charge), generation costs would be expressed in a kWh charge that combined capacity and energy. This would likely include all residential and small commercial customers. For classes that currently pay for demand and energy separately, generation costs would also be expressed separately as demand and energy. Generally, this will be larger commercial and industrial (C&I) customers.[3]

Developing generation rate elements as described above requires three types of data: (1) unit costs for generation capacity and energy; (2) class demand and energy use patterns, or load profiles; and (3) system loss factors by voltage level of service. For unit costs, we would use recent historic market prices in New England for capacity and energy. Given the expectation that the NEPOOL product markets will be operable by year-end 1998, the clearing prices in the relevant capacity and energy markets may provide adequate unit cost data. If all of the product markets are not operable by then, or if they are not

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[2]This process determines rate structure only. Rate level is determined by supplier bids.

[3]Maine C&I customers typically pay separate kW and kWh rates if their demand exceeds 50 kW; kWh rates only if their demand does not exceed 20 kW. For C&I customers between these points, the rate structure varies from utility to utility.

sufficiently stable, another source of published market price data, such as *Power Markets Week*, would be used. For class demand and energy use patterns, we would use T&D utility-provided data.

Because of the requirements of the Commission's load profiling rule, Chapter 321, utilities may have recent data available in time for this purpose; if their load research is not complete, we would use the most current, available data. Finally, T&D utilities would also provide their system loss factors by voltage level of service. These sets of data would allow us to develop generation costs by customer class and usage component for each T&D utility, creating the template for standard offer rates.

2. Request for Comment

As noted above, the issue of standard offer rate design attracted little comment in the Chapter 301 rulemaking. Thus, before proceeding to the data gathering phase of this investigation, we ask for comment on the approach presently contained in the Rule, and further described above. Specifically, we seek comment on how well the approach comports with the objectives noted in section II and on how practically it can be administered. We also invite and seek comment on alternative approaches consistent with Chapter 301, which would establish the unbundled generation rate elements differently. Finally, we ask for comment on the specific items listed below:

1. How will potential standard offer suppliers perceive/react to the constraints imposed by the approach described above? Will it tend to discourage bidders? Will it tend to increase standard offer rates relative to approaches wherein providers set their own rate designs?

2. Are the unit costs for generation described above appropriate? Obtainable?

3. Please comment on to what extent standard offer rates should vary by season or time-of-day.[4] If standard offer rates do vary by season or time-of-day, should the pattern conform with current bundled electric rates, or with expected market supply costs? Include comment on possible implications of this issue for T&D rate design and whether such implications are acceptable. For instance, a standard offer rate that does not vary by season could require maintaining or increasing seasonal

[4]By this we are not referring to the total electricity prices standard offer customers will pay, which may reflect differentials of T&D rates, but only the standard offer component.

differentials in T&D rates to preserve rate stability overall for standard offer customers. Is such a result acceptable?

4. Please comment on to what extent standard offer rates should incline or decline with usage. Are flat or declining rate structures for standard offer service desirable? Alternatively, should standard offer rates track the block structure(s) in current bundled rates? For CMP, should the standard offer rate design for Rate A follow the block structure pattern of CMP's current Rate A? If so, please comment on the implications to standard offer providers, given that the rate structure may not match suppliers' cost structures. If not, please comment on the implications for T&D rates. For example, would CMP's T&D Rate A have to incline more steeply than the current rate in order to preserve rate stability overall for standard offer customers? Is such an outcome desirable? Acceptable?

B. CMP Proposal; Variation

1. Description

In testimony filed in Docket No. 97-580, CMP proposed an alternative approach to standard offer rate design. (Updated and Rebuttal Testimony of Paul A Dumais, Lindley S. Peaco and Hethie Parmesano, June 26, 1998.) As we understand CMP's proposal, suppliers would compete on a customer class-by-class basis to provide standard offer service. Thus, the bids themselves would provide a market measure of the generation cost for each rate class of the T&D utility. Standard offer service within a T&D service territory could be provided by several different suppliers; in theory, a different supplier for each class.

There are aspects of CMP's proposed approach we view as preferable to the Chapter 301 approach; there are also aspects that raise concerns or questions. An obvious benefit to CMP's approach is that it provides a market measure of generation costs by customer class. Foremost among our concerns about the approach is that it would be difficult, perhaps impossible, to ensure that standard offer bids are received for all customer classes. In addition, carving up utility service territories could diminish the attractiveness of Maine's standard offer market to providers. This market is likely to be valued by suppliers at least in part because it is (a) large; and (b) diverse. Because profit margins in the emerging competitive electricity market are expected to be small, the size of the capturable market will likely be important to suppliers.

Also, because suppliers will have an all-requirements obligation to serve their share of the standard offer load, and because this load will be hard to predict, its diversity should serve to reduce risks relative to serving discrete customer types.[5] There may also be increased administrative complexity and cost associated with this approach. Finally, unless the Commission prescribes rate design within class, if bidders propose different structures they will be difficult to compare objectively. Nonetheless, because of its positive features, we ask for comment on CMP's proposal and the concerns we note above.

Finally, there is a variation on CMP's proposal that warrants consideration. Suppliers would bid as contemplated by Chapter 301 for the entire standard offer load (or a percentage thereof); however, each supplier would propose rates by customer class rather than according to a Commission-set rate design template. To ensure compatibility with the T&D utility's rate structure and with its metering and billing capability, the Commission could prescribe the required or allowed rate elements for each customer class, and allow suppliers to propose rates for each element. For example, the Commission could require that suppliers bid kWh rates for residential classes, and allow suppliers to bid demand and kWh rates for larger commercial and industrial classes. If there were advantages to further specify rate structures within classes, the Commission could do so, such as by requiring standard offer rates to track current proportional relationships among rate elements within a class. An approach like this could provide suppliers with more flexibility to match expected costs and revenues, while also leaving the Commission with some ability to manage the pattern of standard offer rates within classes.

2. Request for Comment

We ask for comment on CMP's proposed approach and the variation described above. We would find it particularly helpful for commenters to compare the merits of these approaches with the Chapter 301 approach and note their attributes with respect to the objectives noted in section II: continuity for customers, and simplicity and objectivity in bidding and selection. In addition, we ask commenters to address the following specific issues with respect to these approaches:

1. How would bids reflecting varying rate designs be compared? Could the lowest overall bid be determined by using a specified set of billing units, such as total billing units in the prior calendar year? If total billing units are not appropriate, for example, because they may not reflect likely

[5]This may be more true for some classes than others.

standard offer usage, what set of billing units could be used to compare bids?

2. If multiple suppliers are chosen, each with a different rate design, what rates would standard offer customers pay? Based on what rates and, more importantly, what usage would each supplier be paid?

3. Would supplier-proposed rate designs be likely to track the supplier's expected costs for each class? Please explain why or why not, as well as the implications if rates do not track costs.

IV. PROCEDURE

We are initiating this investigation pursuant to 35-A M.R.S.A. § 1303 and Chapter 110, Part 7. All electric utilities in the State are parties to this proceeding. Interested persons may file petitions to intervene by October 23, 1998. The petitions must state the person's interest in the proceeding and be mailed or faxed to:

Dennis L. Keschl, Administrative Director
Maine Public Utilities Commission
242 State Street, 18 State House Station
Augusta, Maine 04333-0018

Persons wishing to monitor the proceeding by receiving Commission documents may request to be placed on the Commission's interested person list by notifying the Administrative Director.

Comments on the issues raised in this Notice must be filed by November 4, 1998. Reply comments must be filed by November 16, 1998. After reviewing the comments, the Commission will determine further procedures to complete this investigation.

Dated at Augusta, Maine this 14th day of October, 1998.

BY ORDER OF THE COMMISSION

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Dennis L. Keschl
Administrative Director

COMMISSIONERS VOTING FOR: Welch
Nugent
Diamond